Agriculture Financial Services Corporation's (AFSC)

QUARTERLY REPORT

2015-16

(Second Quarter Update - September 30, 2015)

AFSC is in the business of helping Albertans achieve prosperity and build successful businesses.

Second Quarter Update – as of September 30, 2015
Agriculture Financial Services Corporation

Nature of Operations

Agriculture Financial Services Corporation (AFSC) is a crown corporation that is in the business of helping rural Albertans achieve prosperity and build successful businesses. Through strategic risk management and income stabilization programs for farm clients, and forward-thinking lending programs for both urban and rural entrepreneurs, AFSC provides Alberta businesses with the valuable tools they need to thrive.

Overview

Economic Climate

Difficulties in the energy sector continued to dominate the provincial economic environment. Fears of slower Chinese economic growth and a glut of international oil supplies dominated international markets. In response, the price of Crude Oil (WTI) dipped to a low of $38.22 USD/bbl in August and is forecasted to remain low over the next quarter. Whereby Alberta's other major sectors performed well over the quarter, this performance has been overshadowed by the underperforming energy sector. Due to the energy sector slow-down, the employment composition of the province has begun to change. There has been a shift away from high paying jobs in the energy sector to employment in other industries. This labor market shift may help to ease labour challenges faced by agricultural producers.

World agricultural prices for heavily traded commodities such as corn and soybeans have fallen from the historic highs reached in 2013. The low Canadian dollar and diversity of crops produced in Alberta, created local stability in domestic row crop prices. Cattle markets, however, experienced significant downward pressure near the end of the quarter. Even though this pressure has trickled down the entire cattle supply chain, prices remained significantly stronger than this time last year. The fall in cattle prices has been more pronounced in the United States as the low exchange rate has provided support for Canadian cattle prices. Over the quarter, the dollar reached a low of USD $0.7455 and is expected to remain low over the next quarter.

Annual crop conditions

The start of the second quarter saw crop development conditions and moisture ratings vary across the province and these continued to be significantly affected by the hot and dry weather. Starting in the middle of July, most agricultural areas began to return to normal rainfall accumulations, improving crop conditions throughout most of the province.

By August, harvest was underway with swathing of some crops and combining, particularly for dry peas, started in some areas. The first frost was reported in northern areas during the August 21-22 time period.

By the start of September, harvest progress was estimated at 21 per cent harvested, approximately one week ahead of the long term average and ahead of 2014's 13 per cent harvested. Wet weather during the month slowed down or completely halted harvesting operations across the province. The first killing frost affected 60 per cent of the province with temperatures well below -2 degrees Celsius on September 21st.

By the end of September about 99 per cent of dry peas, 87 per cent of canola, 80 per cent of spring wheat, 76 per cent of barley and 60 per cent of oats were either harvested or in the swath. This is compared to 99 per cent of dry peas, 68 per cent of canola, 76 per cent of spring wheat, 68 per cent of barley and 58 per cent of oats in 2014.

While September rainfall was beneficial for fall seeded crops with 62 per cent of fall seeded crops rated as good to excellent, it created potential issues with the quality of crops still un-harvested.

Additionally, the wet weather slowed harvest progress but helped with the soil moisture conditions. Provincial soil moisture ratings increased from 21 per cent rated as good to excellent at the start of the quarter to 59 per cent by the end of September, below the 74 per cent rated as good to excellent in 2014. Subsoil moisture was rated at 25 per cent good to excellent and increased to 52 per cent by the end of September, compared to 74 per cent in 2014.

Perennial crop conditions

By the middle of July, despite limited plant growth, first cut dryland hay was 70 per cent complete. Haying was almost complete by mid-August with preliminary average provincial yields on dryland estimated at 0.8 ton per acre. This is a decrease from the 1.7 ton per acre a year ago. Grasshoppers were a significant problem in the North East, North West and Peace Regions.

At the end of August, approximately 55 per cent of the province indicated there would be a second cut for dryland hay crop with 16 per cent of the dryland crop and 65 per cent of the irrigated crop already baled.

Late summer and fall moisture helped improve conditions in most of the province. Despite this, only 29 per cent of pasture lands were rated as good to excellent compared to 64 per cent at the same time last year.

Corporate

By mid-July a number of counties and municipalities began declaring Agricultural Disasters. To address this, AFSC, along with the Department of Agriculture and Forestry, continued to utilize the Dry Conditions Team to proactively address their concerns. Numerous factsheets and information bulletins were produced to provide information to producers, AFSC staff, stakeholders and the shareholder.

One of the main challenges in the second quarter was the extreme variability of the weather across much of the province. This variability had a significant impact on AFSC's area-based insurance programs.

AFSC representatives attended county and municipal council meetings across the province in order to review how the programs work and how the weather variability had impacted them. AFSC also began a review of the programs to see where any improvements can be made to address these challenges.

AFSC staff continued working with industry groups to design enhancements to the AgriInsurance Program in order to better meet the needs of our clients. These enhancements would include providing unique insurance supports to organic crop growers, malt barley producers, pulse growers, alfalfa seed producers and beekeepers. The goal is to implement these changes for 2016, however, this is dependent on receiving federal approval for the changes. AFSC has been working with the federal government to provide all the information they require for them to cost share the premiums associated with the changes.

The Corporation also began work to explore different ways to collect client feedback and share this information internally with staff to better serve clients. As part of this, significant progress was made on acquiring an online survey tool and the first survey is expected to be launched in the third quarter.

The @AFSC_AB Twitter account was launched in the first quarter and proved to be an incredibly valuable tool in engaging clients and other audiences during the challenging summer conditions. During the second quarter, AFSC launched a Twitter account for the Human Resources department - @AFSCJobs. The account will support recruitment initiatives and reinforce why AFSC has been chosen as one of the Top 100 Employers in Canada every year since 2010. AFSC also began a revamp of the orientation and onboarding for new employees. This is expected to launch no later than spring 2016.

Second Quarter Update

Lending

During the second quarter of 2015 AFSC approved $129.5 million in loans. This is very similar to the $131.1 million loans approved in the second quarter of 2014-15.

The total outstanding loan portfolio grew two per cent in the second quarter to $2.21 billion from $2.16 billion in the first quarter. This was similar to the growth experienced during the first half of 2014-15.

There were 468 loans approved for the second quarter, which is slightly down from the 480 loans approved for the second quarter of 2014-15.

The Lending operating cost for the first half of the year was 0.58 per cent of the loan portfolio. The annual target for 2015-16 year is 1.2 per cent.

Alberta Farm Loans and Revolving Loans were up slightly over the 2014-15 fiscal period, with the Value Added and Agribusiness Program (VAAP) and Commercial loans slightly below 2014-15 levels. The overall loan numbers were up from the 2014-15 fiscal period.

Commercial lending decreased slightly over the last two quarters. In general, AFSC's existing commercial clients have been experiencing the effects of the downturn in the overall economy. This has impacted the Commercial and VAAP arrears, which increased from 5.7 per cent to 6.2 per cent over the previous quarter.

Farm lending through the Alberta Farm Loan Program continued to be strong. Farm loan arrears remained low at 0.5 per cent (2014 – 0.8 per cent). There was not a significant increase in lending requests as a result of the dry conditions during the second quarter, however AFSC continues to monitor this closely.

Under the Specific Loan Guarantee Program for Feeder Associations, AFSC processed two applications in the second quarter totaling $216,447.00. There are currently 21 separate guarantees outstanding under this program for a total of $4.9 million. A review of AFSC's participation with Feeder Associations is underway to enhance the program in light of higher cattle prices.

A total of $183, 434 interest rate rebates were paid out to the Alberta Flood Recovery programs in the second quarter, bringing the total amount paid to $1.05 million.

Lending

	Lending volume for year		Portfolio loans outstanding	
	Number of loans	Amount lent ($M)	Number of loans	Amount outstanding ($M)
2015-16 (2nd quarter)				
Farm	988	242.34	10,927	1,760.52
Commercial	71	38.63	899	278.71
Value-Added and AgriBusiness	40	21.08	415	167.60
Total	1,099	302.05	12,241	2,206.83
2014-15 (Annual)				
Farm	1,777	400.05	10,670	1,634.98
Commercial	172	77.68	926	276.63
Value-Added and AgriBusiness	84	45.14	410	165.88
Total	2,033	522.87	12,006	2,077.49
2013-14 (Annual)				
Farm	1,770	391.59	10,386	1,487.61
Commercial	232	95.54	1,008	302.31
Value-Added and AgriBusiness	102	63.94	405	169.41
Total	2,104	551.07	11,799	1,959.33
2012-13 (Annual)				
Farm	1,857	384.93	9,969	1,366.17
Commercial	258	115.39	1,018	280.97
Value-Added and AgriBusiness	103	52.58	362	142.56
Total	2,218	552.90	11,349	1,789.70

M=Million

Lending Operating Results

	2015-16 Target	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Annual lending volume ($M)	558	302	523	551	553
Loans outstanding ($M)	2,276	2,207	2,077	1,959	1,790
Admin. cost ($M)	24.81	12.43	24.51	22.97	23.01
Write-offs ($M)	**	**	3.5	1.75	8.34
Operating surplus [deficit]	0	2.86	4.51	12.53	[4.00]

M=Million
** To be determined as information becomes available.

Lending Delivery Effectiveness

	2015-16 Target	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Portfolio growth (% year over year)	10	6.2	6.1	9	11
Operating costs (% of portfolio)	1.20	0.58	1.18	1.17	1.29
Write-offs (% of portfolio)	**	**	0.17	0.09	0.47

**To be determined as information becomes available.

Insurance

During this quarter, a number of clients requested that they be able to put their perennial and annual crops to another use as a result of the dry conditions and lack of rainfall in some areas of the province. During the second quarter there were 31 hay and 2,525 crop pre-harvest claims initiated, compared to 60 and 1,508 in 2014 crop year. Haying is complete for the year and generated 586 post-harvest claims mostly due to the reduced yield. This was a dramatic increase from the 164 post-harvest claims in 2014.

Hail was also prevalent during this quarter and resulted in 3,704 Hail Endorsement claims, most of which have been completed and paid out. Due to the harvest delays, wildlife became an issue for many producers. There were a total of 592 wildlife claims, mostly in the northern part of the province.

A total of 5,521 indemnities have been approved and paid out to Alberta farmers. Of those, 4,249 were for Hail Endorsement, 333 for crop pre-harvests, and 377 for post-harvest claims. AFSC expedited payments to clients with area-based insurance programs, which resulted in a payout of $32.1 million in Moisture Deficiency Insurance, $3.1 million to the short season Satellite clients, and $12.1 million on the Silage/Greenfeed Lack of Moisture program.

AgriInsurance Operating Results

	2015-16 Target	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Number of policies	29,618	29,223	29,028	31,028	31,079
Number of acres insured (M)	34.47	35.6	34.96	36	34.87
Amount of risk ($M)	7,134.45	7,402.54	6,799.33	8,611.45	8,991.73
Amount of premium ($M)	611.00	617.74	584.83	780.43	662.57
Amount of admin cost ($M)	39.12	19.18	38.40	34.41	34.47
Indemnities ($M)	N/A	670.26	372.65	308.56	551.20
Loss to premium ratio (%)	N/A	108.56	63.72	39.50	83.20
Operating surplus [deficit] ($M)	N/A	[72.52]	229.03	469.09	102.64

M=Million
N/A = Information not applicable
Note: Insurance performance measures include information for base programs as well as endorsements.

AgriInsurance Delivery Efficiency

	2015-16 Target	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Admin./policy ($)	1,370	656	1,324	1,109	1,108
Admin./acre ($)	1.13	0.54	1.10	0.96	0.99
Admin./risk (%)	0.55	0.27	0.57	0.40	0.38
Admin./premium (%)	6.50	3.11	6.57	4.41	5.20

Straight Hail Operating Results

Many producers decided that, despite the dry conditions, they wanted to ensure they were protected from potential hail damage. This resulted in an additional 622 Straight Hail policies purchased which cover 652,000 acres. This brought the total to $546.5 million in risk generating $45.1 million of premiums for the year. There were also 1,343 claims paid during the second quarter, totaling $31 million. This compares to 2,165 claims and $42 million paid out during the same time last year.

	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Number of policies	3,759	4,648	4,895	5,815
Number of acres insured (M)	3.80	4.84	4.94	5.59
Amount of policy risk ($M)	546.53	711.42	589.83	625.90
Amount of premium ($M)	45.13	56.04	47.00	47.18
Admin. cost ($M)	1.19	2.31	2.22	3.10
Indemnities ($M)	35.10	61.24	37.76	58.52
Loss to premium ratio (%)	78	109	80	124
Operating surplus [deficit] ($M)	6.56	[$8.84]	$4.49	[$8.17]
Market share of straight hail premium (%)	**	60	55	59
Market share of total hail premium (%)	**	90	89	88

M=Million
**To be determined as information becomes available.

Western Livestock Price Insurance Program (WLPIP)

Even though no calf sales take place in the second quarter, policy expirations and assessments started in September. Fed and feeder sales are normally very slow through the summer months.

Policy sales totaled 54 in the second quarter for $17.9 million in liability coverage and $161,813 in premium collected. This compares to 191 policies sold in the second quarter of 2014-15 (a decrease of 137) and $69 million in liability coverage and $1.18 million in premium collected.

Turning to the specific products there were 11 fed policies and 40 feeder policies sold this quarter. In comparison, there were 40 fed policies and 154 feeder policies sold over the same time frame for 2014-15. There were three hog policies sold this quarter. There were also 284 assessments completed in the second quarter with no indemnity payments made. However, the 45 day loss forecast as of September 30th suggested modest payments.

Fed settlement index values saw prices move downward from the highs above $200 per cwt in the first quarter of this year to a value of approximately $170 per cwt. Feeder and calf settlement index values also experienced a similar drop, being more pronounced in the last month of this quarter. While the dollar drop in these markets is significant, it is important to keep in mind how high these markets had climbed over the last two years. In terms of a percentage change it is a move that producers have faced before and will face again.

The downward move in prices witnessed in the second quarter demonstrates how quickly market prices and market conditions can change without any major shock event. The three key elements of price, basis and currency risk were front and center through this highly volatile period and it is these three risk elements that are covered off with WLPIP.

WLPIP Operating Results

	Policy option	Policies	Premiums ($)	Liabilities ($)	Indemnity	Loss to premium
Alberta 2015-16 Second Quarter						
	Calf	1,126	2,097	215,288	**	**
	Fed	22	214	31,359	**	**
	Feeder	347	1,143	77,147	**	**
	Hog	3	4	91	**	**
Total		1,498	3,457	323,884		
Alberta 2014-15						
	Calf	2,566	5,123	358,773	N/A	0%
	Fed	304	2,738	194,913	74	3%
	Feeder	1,875	12,869	695,333	N/A	0%
	Hog	N/A	N/A	N/A	N/A	0%
Total		4,745	20,730	1,249,019	74	0
Alberta 2013-14						
	Calf	1,528	3,454	196,916	N/A	0%
	Fed	1,004	5,021	566,346	2,083	41%
	Feeder	3,454	14,917	1,005,627	1,122	8%
	Hog	16	42	1347	39	93%
Total		6,002	23,433	1,770,236	3,244	14%
Alberta 2012-13						
	Calf	273	489	35,948	946	193%
	Fed	289	1,750	175,951	4,816	275%
	Feeder	1,003	6,240	385,940	17,605	282%
	Hog	6	11	311	8	72%
Total		1,571	8,490	598,151	23,375	275%

**To be determined as information becomes available.
N/A = Information not applicable

AgriInvest

At the beginning of second quarter, producer deposits totaled $535.2 million. By mid-September producer balances increased to $551.8 million but then in the third week of September decreased by $645,813 to $551.2 million. The second quarter finished with a small increase in deposits of $90,218 to a final balance of $551.3 at the end of September with 27,322 producers depositing. Since the inception of AgriInvest in 2007, Alberta producers have received $378.6 million in government funds.

AgriInvest Balance of Funds on Deposit as of September 30

Year	Number of Producers Depositing	Total Value of Contributions by Producer ($) M	Total Value of Contributions by Government ($) M	Amount on Deposit ($) M
2014	17,190	33,067	33,067	551
2013	21,936	61,510	61,510	480
2012	22,652	90,250	90,250	390
2011	22,741	76,969	76,969	316

M=Million

AgriStability

In the second quarter, AgriStability completed the majority of 2013 claims with only one per cent of claims remaining. As of September 30, 2015, for the 2014 program year, 54 per cent of the 11,010 claims received to date have been completed, resulting in a payout of $11.3 million in benefits. The amount of opt outs received in 2014 was half of those received in 2013.

Commodity prices declined late in 2013 but started to see a recovery in the latter part of the 2014 production year. Grain prices saw a moderate increase but did not return to the levels that they were early in 2013. The 2014 year also saw a decline in crop yields when compared to the prior year.

Cattle prices progressively increased during the 2014 year and peaked by the end of the year at record levels. The prices began to level off in early 2015 but still maintain high value.

In the 2014 year hog prices had shown an increase overall, but by the end of the year returned to prices just slightly above the start of the year. In 2015 there has been less of an increase in prices during the summer months compared to what occurred in 2014.

The turnaround time for 2014 claims with payment was 27.7 days. For non-payment claims the turnaround time was 10.7 days.

The average support level decreased from $193,253 in 2013 to $171,190 in 2014. This is the result of the introduction of limited reference margins in 2013.

AFSC AgriStability Cost Effectiveness

	2015-16 (2nd qtr.)	2014-15 (Annual)	2013-14 (Annual)	2012-13 (Annual)
Admin. cost ($M)*	7.97	18.41	18.01	19.07
Less AgriInvest ($M)	-0.83	-1.52	-1.55	-1.77
Net AgriStability admin cost ($M)	7.14	16.89	16.46	17.30
Number of files processed	5892	15,244	17,825	21,458
Cost per file ($)	1212	1,108	923	806

M=Million

* Income Stabilization administrative costs include Alberta's share of AgriInvest administration costs, which Benchmarks do not.

** To be determined as information becomes available.

AgriStability Claims by Industry

Industry	Agristability claims ($M)	Denied AgriStability claims ($M)	AgriStability claims > $0 ($M)	AgriStability ($M)
2014 Program Year (2nd Quarter)				
Livestock	1,472	13	43	0.86
Crop	2,156	18	248	10.42
Other	215	2	10	0.08
Total	3,843	33	301	11.36
2013 Program Year				
Livestock	4,100	78	668	36.01
Crop	7,599	127	990	18.38
Other	904	46	83	2.09
Total	12,603	251	1,741	56.48
2012 Program Year				
Livestock	4,994	138	728	32.00
Crop	8,670	203	561	13.83
Other	1,295	59	135	1.63
Total	14,959	400	1,424	47.47
2011 Program Year				
Livestock	6,586	179	825	23.94
Crop	9,790	352	1,188	19.47
Other	1,570	82	198	5.52
Total	17,946	613	2,211	48.93

M=Million